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September 5, 2000

Non-Proprietary
Per: Charles B. Welch

Charles B. Welch, Jr.

~~Confidential and Proprietary
Information~~

VIA HAND DELIVERY

Mr. K. David Waddell
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Re: Generic Docket Addressing Rural Universal Service
Docket No. 00-00523

Dear Mr. Waddell:

Enclosed for filing, please find the original plus thirteen (13) copies of the Comments of the Rural Independent Coalition in the referenced docket. Copies are being served on parties of record.

If you have any questions or concerns with regard to this filing, please do not hesitate to contact me.

Very truly yours,

**FARRIS, MATHEWS, BRANAN,
BOBANGO & HELLEN, P.L.C.**

Charles B. Welch, Jr.

Charles B. Welch, Jr.

CBW:ccw

Encl:

POSTED
9-5-00

Before the
Tennessee Regulatory Authority
Nashville, Tennessee

REC'D TN
REGULATORY AUTH.

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IN RE:

GENERIC DOCKET ADDRESSING
RURAL UNIVERSAL SERVICE

DOCKET NO. 00-00523
OFFICE OF THE
SECRETARY

COMMENTS OF THE RURAL INDEPENDENT COALITION

on behalf of

Ardmore Telephone Company, Inc.
Ben Lomand Rural Telephone Cooperative, Inc.
Bledsoe Telephone Cooperative
CenturyTel of Adamsville, Inc.
CenturyTel of Claiborne, Inc.
CenturyTel of Ooltewah-Collegedale, Inc.
Concord Telephone Exchange, Inc.
Crockett Telephone Company, Inc.
DeKalb Telephone Cooperative, Inc.
Highland Telephone Cooperative, Inc.
Humphreys County Telephone Company
Loretto Telephone Company, Inc.
North Central Telephone Cooperative, Inc.
Peoples Telephone Company
Tellico Telephone Company, Inc.
Tennessee Telephone Company
Twin Lakes Telephone Cooperative Corporation
United Telephone Company
West Tennessee Telephone Company, Inc.
Yorkville Telephone Cooperative

"The Coalition of Small LECs and Cooperatives"

September 5, 2000

**Before the
Tennessee Regulatory Authority
Nashville, Tennessee**

IN RE:

**GENERIC DOCKET ADDRESSING
RURAL UNIVERSAL SERVICE**

DOCKET NO. 00-00523

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COMMENTS OF THE RURAL INDEPENDENT COALITION

The Rural Independent Coalition (hereafter referred to as the “Coalition” or the “Independents”) respectfully file these Comments in response to the invitation of the Tennessee Regulatory Authority (“TRA” or “Authority”) set forth in its July 14, 2000 Order in the above captioned proceeding and modified by the Notice issued on July 21, 2000. The Coalition membership is comprised of 20 Independent telephone companies and cooperatives which collectively provide approximately 314,000 access lines to customers who reside and work within the more rural areas of Tennessee.

I. Introduction - Resolution of this Proceeding is Essential Prior to Changes in Existing Rate Design and Cost Recovery Mechanisms.

Each of the Coalition members provides universal service within its respective service area and is considered a “rural telephone company” pursuant to the federal Communications Act of 1934 as amended by the Telecommunications Act of 1996 (the “Act”). Each of the Coalition members has been designated an Eligible Telecommunications Carrier (“ETC”) by the Authority and is, accordingly, eligible for federal Universal Service Fund (USF) cost recovery in accordance with the Federal Communications Commission (“FCC”) rules as applied to Rural Telephone Companies. In the case of each Independent, the provision of universal service has been achieved through reliance on the established and existing rate design and cost recovery mechanisms that have been

established under the auspices of both federal and state regulatory policies and rules.¹

Irrespective of whether meaningful market service choice will come to the higher cost to serve (and thereby less potentially profitable) rural service areas of the State, the Coalition members are acutely aware that competitive pressures in the more profitable markets have resulted in pressures on both federal and state regulators to consider changes in rate design, cost recovery mechanisms, access charge levels and both implicit and explicit universal service programs. Ironically, it is the collective impact of these factors that have enabled the Coalition members to advance the provision of universal services in rural Tennessee while concurrently maintaining reasonable local basic service rate levels.

Tennesseeans currently enjoy the benefits of a framework that promotes the continued deployment of comparable basic and advanced services, provided in the most rural areas of the State, offered at rates that are comparable to rates in the more urban areas. If changes in the established cost recovery mechanisms were permitted or imposed in the absence of consideration of the resulting immediate and significant impact on universal services and basic service rates, the results would be severe. The members of the Coalition cannot maintain the provision of universal service in the absence of adequate cost recovery mechanisms. Potential competitive service providers will have no interest in providing service unprofitably to higher cost to serve rural areas and customers. The implementation of piece-meal change in the absence of a comprehensive rural universal service plan will result in a state of telecommunication user “haves” and “have nots.”

The Coalition rural local exchange carrier members, therefore, recommend that the Authority

¹ Although the members of the Coalition that are organized as Cooperatives are not regulated by the TRA for purposes of establishing their basic customer rates, these companies have the same reliance on intrastate toll and access services and interstate access services for overall cost recovery as do other coalition members. The existing rate design and cost recovery mechanisms for interstate access and intrastate access and toll alleviate the pressures that would otherwise exist to raise local service rates to inordinate levels.

establish a State universal service fund (to be referred to as “State USF”) for rural LECs on an expedited basis. The State USF proposed by the rural Independents will establish a framework within which the authority can foster universal service throughout rural Tennessee while concurrently ensuring that reasonable end-user rates and access charge levels are encouraged and maintained. The framework proposed by the Coalition will also address and accommodate additional changes and requirements that will undoubtedly affect service deployment in rural areas. These include investment needs related to advanced service network requirements and unresolved federal proceedings addressing jurisdictional separations, interstate access charges, and rural federal USF. In addition, and as the Authority is aware, the rural Independents and their customers are also confronted by BellSouth’s pronounced intent to modify or terminate established intraLATA toll settlements and the access framework which compensate the Independents for the originating and terminating access services they provide with respect to intraLATA toll services established pursuant to BellSouth tariffs. If the BellSouth IntraLATA toll settlement plan were to be eliminated, rural LECs will lose approximately \$15 million in settlements that currently are part of their overall cost recovery that allows for reasonable basic rates. Revenue losses, in whatever form, will have to be made up from some form of cost recovery if comparable basic rates and service levels are to be maintained. The implementation of the rural State USF and rate design proposed herein by the Coalition would address this concern in an equitable manner that appropriately reflects balanced public interest concerns for all customers and providers within the State.

Accordingly, the Coalition appreciates the expedited consideration that the Authority is giving to the issue of maintaining and fostering universal service in the rural areas of Tennessee served by the Independents. In accordance with the request of the Authority, the Coalition will first address the applicability of the decisions in Docket No. 97-00888 to this docket. The Coalition will then offer a comprehensive conceptual proposal to address universal service concerns within the

rural areas of the State served by the Independents. Finally, the Coalition will address the recent actions by BellSouth that, if not addressed by the TRA or allowed to be implemented unilaterally by BellSouth, would severely impact the ability of the Independents to continue the provision of universal services at reasonable and comparable rates.

II. Coalition Comments and Positions Regarding the Applicability to this Proceeding of the Authority's Previous Decisions in the Non-Rural Universal Service Phases of this Proceeding.

The TRA has completed two Phases of the Generic Docket No. 97-00888, *In Re: Universal Service Proceeding*. In each of these Phases, the TRA has reached decisions with respect to the non-rural Tennessee telephone companies. In Phase I, the TRA addressed processes for identifying "implicit subsidies" and for structuring an intrastate Universal Service Fund for non-rural telephone companies. In Phase II, the Authority analyzed universal service cost models for non-rural telephone companies as a means potentially to determine the amount of support required to implement the decisions reached in Phase I of the proceeding. In accordance with the Authority's request, the Coalition offers the following comments regarding the applicability of the Authority's findings in these proceedings to the consideration of State USF for rural LECs.

A. Phase I Findings

Issue 1: Services to be supported by a Tennessee Universal Service Support System

Finding of the TRA for non-rural Companies: The Authority ordered that the "core" services, with respect to the primary access line to the premises of a residential customer, to be supported by an intrastate universal service fund consist of the dial tone, touch-tone and usage provided for the provision of two-way switched voice or data transmission over voice grade facilities; Lifeline; Link-

Up Tennessee; access to 911 Emergency Services; and educational discounts existing on June 6, 1995.² The Authority determined that Lifeline and Link-up will be funded through a separate fund and that the Tennessee Relay Center and public interest payphones will be addressed subsequently to the extent necessary.

Coalition Position: Universal Service concerns in rural areas extend beyond the core services that have been identified by the TRA for inclusion in non-rural company universal service. Rural area networks and services are not developed on a customer or individual line basis. To the contrary, the mandate to a rural ETC is to deploy a complete network that is available to provide quality service at reasonable rates to support the developing requirements of the rural service area and all of the customers. The costs of providing this network are not affected by whether the use of the network is for a business or residence or whether the service required is for a first or additional line. Demographic and geographic considerations support the inclusion of all classes of users and all lines within the definition of rural telephone service area universal service.³

The Coalition agrees that the Authority's findings in the *Phase I Order* with respect to Lifeline, Link-Up, TRS and public interest payphones are applicable to this proceeding. The Act provides states with the authority to provide for additional definitions and standards to preserve and

² *Phase I Order*, page 12.

³ The Coalition notes that the rural companies have previously provided the Authority with information regarding the additional burden of attempting to identify primary use lines in rural service areas. See Rebuttal Testimony by Steven E. Watkins filed December 2, 1997, in this docket on behalf of the Coalition of Small LECs and Cooperatives at 2-3 ("The cost of providing universal service does not end with one class of customers, or with a minimum amount of service to a customer, to the exclusion of other classes of customers Rather, LECs construct their networks to provide services to all users in their service area.") Subsequent to the issuance of the *Phase I Order*, the FCC has determined that it will not apply any such distinction with respect to the administration of the Federal USF program.

advance universal service within the State.⁴ For example, carriers in the State have been required to provide no charge county-wide extended area service calling in the State. This service has been deemed to be in the public interest and in all respects supports universal service goals. The carriers in the State are providing this additional service without any additional cost recovery.⁵ The provision of county-wide EAS is an example of service costs which also should be addressed with universal service support.

Issues 2 and 3: Eligible Telecommunications Carriers

Finding of the TRA for non-rural Companies: The Authority found that carriers must provide the “core” services identified in Issue 1, and that carriers must offer toll blocking service, access to directory assistance, access to interexchange carriers, and access to operator services. The Authority recognized that under exceptional circumstances a carrier may obtain ETC status for a limited period even if it cannot provide a qualifying service. The Authority further determined that the requirements for intrastate ETC designation should be consistent with the FCC’s interstate requirements, including advertising requirements and facilities requirements.⁶

Coalition Position: In general, the Coalition finds that the Authority’s decisions regarding ETCs should be fully applicable to the designation of rural telephone company service area ETCs for intrastate purposes. The Coalition supports the reasoned approach of applying consistent interstate standards for ETC status including service requirements, advertising, and facilities requirements that ensure that the providing carrier that “owns” facilities will receive the support associated with the facilities.

In this regard, however, the Coalition respectfully submits that the Authority should adopt

⁴ See 47 U.S.C. § 254(f).

⁵ Some interexchange carriers apparently do not honor toll-free county-wide calling.

⁶ *Phase I Order*, pp. 16-19.

additional findings with respect to the designation of ETC status in an area served by a rural telephone company. Specifically, and consistent with §214(e)(2) of the Federal Act, the Authority should acknowledge that a specific public interest finding is required prior to designating multiple ETCs in rural service areas. Congress incorporated the right and obligation of a State regulatory authority to give distinct consideration to the designation of ETCs in rural service areas because of its recognition of inherent distinctions in the higher cost to serve less populated markets and the overall effect on continuing availability of quality services at reasonable rates.

The ramifications of designating multiple ETCs in the more robust competitive service areas served by non-rural telephone companies is in its initial observation stage. Designation of additional ETCs in the rural service areas should not result in, or encourage, counter-productive results. Competitive carriers that deploy network and services on a selective basis to only the lowest cost or the most lucrative customers should not be rewarded with interstate and intrastate USF funds. Policy must be balanced to ensure cost recovery for the incumbent rural ETCs that may otherwise remain committed to the provision of network and services fully throughout their respective service areas. Cost recovery is necessary to support ubiquitous networks that are designed to provide continued advanced services at reasonable rates. Accordingly, the Coalition respectfully urges the Authority to adopt prudent policies that do not discourage the investment in network to provide advanced service to all subscribers residing throughout rural service areas of Tennessee.

Issue 4: Carrier of Last Resort Designation

Finding of the TRA for non-rural Companies: The Authority determined that the designation of carrier of last resort set forth in state law remains relevant, “and in service areas where only one ETC exists, the term as contemplated by statute is applicable.”⁷ Where multiple ETCs exist, the Authority found that the FCC’s exit requirements (set forth in §54.205 of the FCC’s Rules and

⁷ *Phase I Order*, p. 21.

Regulations) sufficiently address the carrier of last resort obligations required by TCA §65-5-207(a).

Coalition Position: The Coalition agrees that this finding is applicable to the rural telephone companies. In fact, the Coalition submits that it is, to a large extent, the Carrier of Last Resort Obligations undertaken by the rural incumbent ETCs serving the less market driven areas of the state that give rise to the need for careful consideration of a comprehensive rate design and state universal service plan for rural telephone companies and their subscribers. The public interest issues associated with ETC designation for rural service areas (as explained above) and carrier of last resort considerations converge with respect to rural telephone company areas.

Issue 5: Service Area for ETCs

Finding of the TRA for non-rural Companies: The Authority found that service areas for non-rural telephone companies should be designated by wire center.⁸

Coalition Position: The Authority properly did not apply this finding to rural telephone companies. Under the §214(e)(5) of the Federal Act, “service area” means the rural company’s “study area” until such time as the FCC and the States (after Joint Board consideration) establish a different definition. Within the context of this definition of “service area,” the Coalition notes that, depending upon the Authority’s decisions in this proceeding, the public interest may require implementation of disaggregated (i.e., deaveraged) support in rural areas. In the event that the Authority established an intrastate support mechanism for rural companies that provides support on a per-line basis, there must be recognition of the fact that within a rural service area there are likely to be customers or service zones with costs that are below the average cost and others with cost much higher than the average. Under these circumstances, if per-line support does not reflect these differences from zone to zone, the support mechanism would encourage a competitor to enter the service territory on a selective basis in an effort to obtain per-line support calculated on an average

⁸ *Phase I Order*, p. 23.

basis across the study area while serving only those areas and customers for which the cost of service is below the average. Under such conditions, a carrier could receive unwarranted high cost network support in areas and for customers that are not necessarily high cost. The adoption of the comprehensive proposal set forth in Section III, below, would avoid this potentially counter-productive outcome.

Issue 6: Contributors to the Tennessee Intrastate Universal Service Fund

Finding of the TRA for non-rural Companies: The Authority found that, with two exceptions, “all providers of intrastate telecommunications services in Tennessee, regulated or not, shall be required to contribute to the intrastate USF.” The Authority provided a temporary exception for rural telephone companies and cooperatives “as long as the rural carrier or cooperative is not serving non-rural customers and has not entered into an interconnection agreement to serve non-rural customers.” The Authority also established a *de minimis* exemption with a \$1,000 contribution threshold.⁹

Coalition Position: The Coalition agrees that the Authority’s finding is applicable to this proceeding. The proposal set forth by the Coalition in Section III, below, would parallel the federal USF approach, is consistent with the TRA’s previous finding, and would extend the conceptual approach to the rural telephone company plan.

Issue 7: Affordability of Rates

Finding of the TRA for non-rural Companies: The TRA found that there was no reason to build affordability standards into revenue benchmarks for non-rural telephone companies or to tie state USF to subscriber income.¹⁰

Coalition Position: The Coalition agrees that this finding is applicable to rural telephone

⁹ *Phase I Order*, p.27.

¹⁰ *Phase I Order*, pp. 30-31.

company service areas. Moreover, this finding may be additionally useful to the Authority's consideration of universal service concerns in rural telephone company areas. As set forth in §254 of the Federal Act, the provision of universal service requires consideration not only of "affordability," but also of "comparable" rates. When establishing policies to promote universal service in rural company areas, it is imperative not only that rates be "affordable," but also that rates and services offered in rural areas be "comparable" to those offered in more urban areas. The proposal set forth by the Coalition in Section III, below, incorporates both the Authority's finding and the concepts of rate comparability and affordability to establish a rate design that meets universal service objectives in rural areas.

The Coalition also agrees with respect to the Authority's decision not to consider income levels. The matter of income levels and related concerns is better addressed through Lifeline and Link-Up programs.

Issue 8: Implicit and Explicit Subsidies

Finding of the TRA for non-rural Companies: The Authority found that for non-rural companies, "a subsidy occurs when the costs associated with at least one good or service exceeds its revenue, while the revenues from the sale of some other set of goods or services exceed the associated costs, such that the total costs are recovered."¹¹ The TRA further determined that an implicit subsidy is one hidden in the costs, while an explicit subsidy is "a set payment that covers costs in excess of revenues for certain goods or services provided."¹² In addition, the Authority found that a group of services is receiving a subsidy "if the associated forward-looking economic costs exceed the revenues from the sale of the services."

Coalition Position: These conceptual aspects of the non-rural telephone company Universal

¹¹ *Phase I Order*, p. 33.

¹² *Id.*

Service Proceeding are not currently applicable to rural telephone company universal service considerations, and the relevance and application of these concepts is not immediately apparent or necessary. At the Federal level, with respect to models of so-called forward-looking costs, accuracy and other problems with respect to application to rural telephone companies have been well discussed and established. A Rural Task Force established by the FCC is reviewing this matter and preparing recommendations for consideration by the FCC. The Coalition respectfully submits that consideration of economic analysis and academic theories do not resolve the actual service deployment concerns and pressures or the practical network cost recovery for rural telephone companies that exist today and must be addressed by any effective plan. Accordingly, the Coalition suggests that universal service considerations for a rural telephone company should be based on the actual costs incurred and the actual network cost recovery required to achieve a successful universal service result.

Rural companies recover their actual costs of providing universal service through rates charged for basic service, intrastate access service (including an intraLATA plan with BellSouth), interstate access service, and Federal USF. If the total cost recovery from these sources, established at affordable and comparable levels, do not generate revenues sufficient to recovery the rural company's costs, the company will require an additional cost recovery mechanism. The proposal set forth by the Coalition in Section III below applies this principle and establishes a mechanism to explicitly identify cost recovery that must be provided from a State USF for rural companies.

Issue 9: Revenue Benchmark and Preliminary Cost Modeling Issues

Finding of the TRA for non-rural Companies: The authority found that for non-rural companies, the revenue benchmark used should be average revenue per line for a particular wire center when determining state support for that wire center. The Authority also found that a generic

cost model should be adopted for all non-rural companies.¹³

Coalition Position: This aspect of the Authority's findings in the non-rural generic proceeding is not currently applicable, in a direct sense, to universal service concerns in the rural telephone company service areas. The basis for the inapplicability of this aspect of the non-rural proceeding to rural telephone companies is incorporated, in part, in the Coalition Position on Issue 8 set forth above. Moreover, the Coalition notes that its position is further supported by the recent decision by the US Court of Appeals for the 8th Circuit which overturned the FCC's forward-looking cost rules known as "TELRIC." The Court noted that cost development could not be based on a hypothetical network.¹⁴

In general, and unlike the non-rural companies, rural incumbent telephone companies face many unsettled issues with respect to changes that will likely disrupt the traditional rate design and cost recovery mechanisms that have been established to provide a reasonable opportunity for a rural company to recover its total costs through a combination of the rates it charges for intrastate and interstate services. When and if such matters as jurisdictional separations, federal rural company USF, and interstate access "restructuring" become finally settled for rural companies, the utilization of benchmarks and cost models may be reconsidered with respect to their applicability to rural companies. In the interim, and as discussed above, rural telephone companies must address both the challenges of uncertain federal regulatory changes and pressures for change in the context of the actual costs they incur and investment they must make to provide universal service in their rural service areas. The proposal set forth in Section III below by the Coalition not only addresses these current requirements, but also establishes the context within which potential change can be

¹³ *Phase I Order*, pp. 36, 40-41.

¹⁴ *Iowa Utilities Board v. Federal Communications Commission*, 2000 WL 979117 (8th cir., July 18, 2000)

anticipated and incorporated on an ongoing basis according to an administratively feasible and practical approach.

Issue 10: How should the TRA determine the basis for support for “low-income consumers?”

Issue 11: Support for Schools and Libraries

Issue 12: Support for Health Care Providers

Issue 13: How should the TRA monitor provision of supported service to determine if support is being used as intended until competition develops?

Issue 14: Are any changes in state laws or rules needed?

Coalition Position: The Coalition agrees with the Authority’s findings regarding Issues 10-14, and submits that no additional consideration of these matters is currently required in the context of this proceeding.

Issue 15: Should the access reform issues be incorporated into the schedule addressing Phase II of the Universal Service Proceeding?

Finding of the TRA for non-rural Companies: In the *Phase I Order*, the Authority indicated that this matter “was addressed prior to the hearing on Phase I.”¹⁵

Coalition Position: Consideration of changes in access structures and rates is both critical and essential to the consideration of universal service concerns for rural telephone companies. Rural telephone companies are currently subjected to immense pressures to reduce both interstate and intrastate access charges (including intraLATA toll contractual settlements).¹⁶ Changes to access charges, however, cannot be achieved in a vacuum. Traditional rural telephone cost recovery has been based on a rate design that maintains reasonable local rates, in large part, through reliance on cost recovery from access charges. This rate design reflects the significant importance of

¹⁵ *Phase I Order*, p. 52.

¹⁶ See Section IV, below, regarding the impact of BellSouth’s announcement of its unilateral intent to terminate current settlement contract arrangements and the relationship of this unilateral intent to this proceeding.

interexchange toll calling in maintaining reasonable rate levels. In addition, the existing rate design reflects acknowledgment that the value of the rural telephone company network is not only enjoyed by the rural subscriber, but also by the entire nationwide network of subscribers that can call and receive calls from end users located in rural areas. The establishment of reduced access charges and resulting reduced access revenues will immediately place pressure on local rates in the absence of a State USF to address any cost recovery dislocation associated with access charge changes.¹⁷

B. Phase II Issues

In general, the Phase II findings address the universal service cost model questions and issues for non-rural telephone companies. It has been the general understanding of policymakers and industry participants that the models are inapplicable to rural telephone company service areas under existing conditions. At the interstate level, the FCC, like the Authority, has acknowledged the distinctions that exist with respect to Universal Service considerations in rural telephone company service areas. The FCC has not applied models to the service areas of these companies and, before considering any changes in rural interstate USF, it will review the findings of a Rural Task Force that it established to consider this matter. Although the findings in Phase II are generally inapplicable to the rural companies because of the focus of these findings on cost models, the Coalition will comment on certain pertinent aspects of the Phase II decision in its discussion of the issues that follow below.

Issue 8c: How does the TRA make implicit support explicit as defined by the Act and the FCC?

Finding of the TRA for non-rural Companies: The Authority determined that “the minimum Universal Service support is the total difference between the cost and the revenue benchmark

¹⁷ The establishment of county-wide EAS calling has already put cost recovery pressure on basic service rates because access revenues have been lost and network costs have increased for the provision of what is free calling.

summed over the wire centers in which cost exceeds revenue, less federal support.”¹⁸

Coalition Position: For rural telephone companies, where models are not applicable, the minimum revenue from a State USF should be equal to the rural company’s total intrastate cost of providing universal service reduced by the revenues it receives from the provision of local and intrastate access service at affordable and comparable rates.

Issue 16: What cost model or method should be adopted to calculate the needed universal service support?

Finding of the TRA for non-rural Companies: These findings address numerous issues regarding the models under consideration for non-rural telephone companies

Coalition Position: The Coalition emphasizes that no aspect of the findings regarding models developed for non-rural telephone companies are applicable to the rural company service areas and the real costs incurred to provide service in these area. For example, the Authority’s consideration of imputed corporate expense reductions and rate of return findings are inapplicable to the real experience in rural telephone company service areas where increasing universal service and network needs, in the context of an uncertain regulatory environment, increase pressures on both expenses and the cost of capital.

Issue 17: How will contracts between LECs be treated?

Finding of the TRA for non-rural Companies: The Authority deferred this issue for consideration in this (rural USF) proceeding.¹⁹

Coalition Position: Contracts related to the provision of universal service between a rural telephone company and another carrier should be treated as follows: revenues to the rural telephone company should be treated similarly to revenues derived from rates charged for universal service;

¹⁸ *Phase II Order*, p. 12.

¹⁹ *Id.*, p. 53.

expenses charged to the rural company should be treated as a cost of providing universal service.

Issue 18: During the transition period should rates be rebalanced? If so, how? How will the TRA handle financial effects on carriers who have been providing support to existing systems?

Finding of the TRA for non-rural Companies: The Authority deferred this issue for consideration in Phase III of the non-rural USF proceeding.²⁰

Coalition Position: In accordance with the Coalition proposal set forth in Section III below, the TRA can establish affordable, comparable levels for rates of both basic and access services. The State USF for rural telephone companies can be derived utilizing the application of these rates, as more fully described below.

Issue 19: Should the TRA adopt new telephone quality of service standards?

Finding of the TRA for non-rural Companies: The Authority determined that a rulemaking should be initiated to establish new standards.²¹

Coalition Position: The Coalition welcomes consideration of standards in rural service areas. The Coalition members have a proven record of provision of quality advanced network services and intend to maintain this ongoing commitment. The Coalition respectfully notes that changes in standards may have ramifications on the cost of providing universal service and the level of state USF that is required to meet the standards that evolve.

Issue 20: How will the affordability of rates be monitored in the future?

The Coalition agrees to work with other members of the Industry and the TRA in a study to examine penetration of service in the State. The Coalition also agrees that the informal and formal complaint process of the TRA is adequate to address affordability complaints. In addition, the Coalition agrees that the TRA's existing Lifeline and Link-Up programs are sufficient currently to

²⁰ *Phase II Order*, p. 54.

²¹ *Phase II Order*, p. 58.

ensure affordable basic local telephone service for properly identified low-income consumers.

Issue 21: What should be the sources of support in a TN Universal Service Support System?

The Coalition agrees that the Authority's findings are applicable in this proceeding. Consistent with the requirements of the Federal Act, universal service should be supported in an equitable and nondiscriminatory manner. The Coalition proposal set forth in Section III, below, contemplates the creation of a fund based on an assessment on all intrastate end user revenues for telecommunications services.

Issue 22: How may universal service support contributions be recovered by the carriers/providers making them? Can carriers contributing to the universal service fund recover those payments and if so how? And

Issue 27: Should carriers' contributions to the USF be passed on to consumers, and if so, should the charges appear explicitly on the consumer's bill?

The Authority joined its findings with respect to Issues 22 and 27, and determined that carriers contributing to a state USF should be able to recover their contributions from customers.²²

The Coalition agrees with this conclusion and believes that this finding is equally applicable to a State USF for rural companies.

Issue 23: How should the transition from the current system to the new systems take place?

The Authority deferred this issue for non-rural companies to Phase III of the non-rural proceeding. The plan proposed by the Coalition in Section III below contemplates that the Authority will determine a reasonable transition period for the resulting changes in rate design and cost recovery.

Issue 25: How will the TRA make sure the universal service system is nondiscriminatory and competitively neutral?

The Coalition agrees with the findings of the Authority that no specific guidelines to address competitive neutrality or nondiscrimination are needed because the TRA's existing statutory

²² *Phase II Order*, p. 62.

authority, rules, and complaint procedures are adequate to address future disputes on these points.²³

Issue 26: When will universal service be addressed again?

The Coalition agrees with the Authority's finding that the Authority has the option to re-evaluate the State USF plan and its ongoing effectiveness at any time. The Coalition proposal set forth in Section III below provides a framework that the Authority can utilize to address the dynamic nature of the network and service changes in the telecommunications industry and the resulting impact on universal service.

Issue 28: How should the cost of providing Lifeline and Link-Up services be determined and recovered?

The Coalition agrees with the Authority's finding that the intrastate cost of Lifeline should be determined by multiplying the number of Lifeline customers by the interstate Lifeline credit of \$3.50 for the Rural Telephone Companies. The Coalition notes that appropriate changes may be required if and when the interstate subscriber line charge is increased for the rural company customers.

III. The Rural Independent Coalition Proposed Universal Service Rate Redesign Plan.

The Tennessee Rural Independents have developed the Tennessee Universal Service Rate Redesign Plan in order to achieve the dual objectives of advancing universal service objectives and principles consistent with the Telecommunications Act of 1996 in a manner that also responds to the concerns of the Independents' access customers regarding the level of access charges and resulting impact on intrastate long distance rates. At the same time, the Coalition members seek to ensure that they each have the opportunity to maintain reasonable basic rates of all of their subscribers and continue to maintain a revenue cost recovery stream that enables continued investment and maintenance of their universal service networks and advancing service offerings.

²³ *Phase II Order*, p. 69.

Accordingly, the plan sets forth a proposal for rate design restructuring that incorporates measured reductions in access charges and the implementation of a State USF. The adoption of the Tennessee Rural Independent Company proposal will serve the long term interest of all Tennessee telecommunications users and thereby serve the public interest, as demonstrated below:

A. Adoption of the Universal Service Rate Redesign Proposal Will Ensure The Provision of Universal Services At Reasonable Rates in a Manner Consistent with the Principles Set Forth in the Telecommunications Act of 1996.

The Universal Service Rate Redesign proposal is a statewide plan for universal basic service rate design and cost recovery that addresses and adopts changes in the telecommunications industry including, but not limited to, changes in the access environment for the provision of intrastate toll service in Tennessee, the provision of intraLATA equal access, and the ongoing evolution of issues related to the FCC's consideration of universal service, jurisdictional separations, and access structure changes.

In order to ensure that the interests and needs of all rural Independent subscribers are addressed, the Universal Service Rate Redesign plan was developed to achieve the following objectives:

- (1) The implementation of a rate design for regulated services, including basic services and intrastate access charges, that does not result in either: a) unreasonable basic rates for rural subscribers; or b) the establishment of an excessive level of access charges which would encourage uneconomic bypass and/or discourage the provision of competitive long distance services to all areas of the state.
- (2) The adoption of a plan that provides rural Independents with the ability to shift revenue recovery embedded in the current implicit support mechanisms to explicit support from the State Universal Service Fund, consistent with the requirements and principles set forth in §254 of the Telecommunications Act of 1996.
- (3) The establishment of a rate design for regulated services, including basic services and intrastate access charges, which permits an individual rural Independent flexibility to respond in an administratively and economically efficient manner to the unique needs of its individual service area and subscribers.

The Universal Service Rate Redesign plan achieves these objectives by establishing a

rational transition for rate adjustments that will continue to ensure the provision of universal services in rural areas of Tennessee at rate levels that are reasonably comparable to rates charged for similar services in urban areas. Concurrent with the transition of basic service rates and access charges, the proposal provides for the establishment of a State USF to provide specific and predictable cost recovery support to the rural Independents to preserve and advance universal service in the areas of Tennessee served by the rural Independents.

B. The Proposed Adjustments In Service Rates and Establishment of a State Universal Service Fund Is Consistent With The Public Interest, the Policy Established by the Telecommunications Act of 1996, and the Tennessee Act.

In order to achieve the purposes and meet the objectives set forth above, changes in the level of intrastate access charges and basic service rates are required. The cornerstone of changes to basic service rates will be to ensure the maintenance of reasonable and "comparable" rate levels. The requirement for changes in rate levels and funding mechanisms, as addressed below, will result from the implementation of changes in the access charge levels.

1. Basic Service Rate Level Benchmark

The Telecommunications Act requires that the rates charged by carriers serving the more rural areas of the State, and the services provided to these areas, should be comparable to the rates and services available in the more urban areas of the State. Accordingly, the Tennessee Rural Independents propose to establish transitional benchmark basic service rate levels comparable to customer rate levels charged in other areas of the state.

In evaluating the overall State USF cost recovery support for any LEC, including any reduction in access charge levels, the benchmark rates will determine the assumed portion of cost recovery to be obtained from basic service rates. The plan will ensure that no LEC will be required to establish rates higher than the benchmark rates. This result will foster the provision of universal service at comparable rates throughout the service areas of the rural Independents. The Coalition

envision the establishment of a transition period for the presumed shift of cost recovery to benchmark levels for those carriers with rates currently below the established levels.

No LEC would be required to raise rates to the benchmark levels, but would have the option to do so. However, in the calculation of State USF support, it will be presumed that cost recovery from basic service rates is at the benchmark levels.

2. Reductions to Access Charge Levels

Concurrent with the consideration of benchmark basic service rates and transitional adjustments to basic rates for some LECs, the access charges of the rural Independents will be adjusted on a transition basis to a level at parity with a rural Independent's interstate access charges. Changes in access charge rates will be initiated concurrently with the establishment of funding from the State USF. A transition of reductions in access charges will result in a more prudent overall relative cost recovery from basic and access services and will accommodate a more uniform competitive intrastate long distance service marketplace. Reductions in access rates will also address the movement of implicit support theoretically incorporated in current access rates to an explicit support mechanism; i.e., the State USF.

3. State Universal Service Fund

The differential between a company's base year intrastate revenues and the level of revenues that would be generated by the application of the transitional benchmark rates and switched intrastate access charge (including adjustments to access rates) established during the transition period and thereafter will be recovered through funding from the State Universal Service Fund. Each rural ETC will utilize its 1999 historical intrastate annual revenues as its intrastate base revenue requirement, or a rural ETC may subsequently choose to apply FCC Part 36 rules to its then current investment and expense levels in order to determine its intrastate revenue requirement to be utilized in lieu of its base year intrastate revenues.

Residual cost recovery from the State Universal Service Fund is consistent with the mandates and specific requirements of the universal service policies set forth in Section 254 of the Telecommunications Act. The 1996 Act requires that existing implicit universal service support mechanisms be replaced by explicit universal service support mechanisms. The Act further requires that explicit support should be specific and predictable, and all telecommunications providers should make equitable and nondiscriminatory contributions to such support mechanisms. This mechanism is also consistent with the universal service policies set forth in the Tennessee Act, Tenn. Code Ann. § 65-5-207(a).

The administration of the State USF can be accomplished by the implementation of mechanisms similar to that used to administer the Federal USF. The Coalition understands that the administration of the state USF is subject to an advisory that the Authority has received from the Attorney General. In the event that the Authority proceeds with internal administration of the State USF, it may find it desirable to separate this ministerial administrative function from its rulemaking, oversight, enforcement, and adjudicatory functions.

As with the Federal USF program, the State fund administrator will project an annual funding requirement based on data provided by recipients - the incumbent rural ETCs and any additional ETCs designated by the Commission. The administrator will be required to develop appropriate rules and procedures consistent with all applicable rules and regulations, subject to the approval of the Authority. Consistent with the public policy goal of universal service and the resulting benefits to all subscribers throughout the state, the revenues for the fund will be generated by the establishment of an assessment on the intrastate end user retail revenues of all companies providing telecommunications services in Tennessee. Each contributing telecommunications carrier will be permitted to recover the contribution made to the State USF from their end users. One competitively neutral means of providing this recovery would be through the establishment of a

State USF charge.²⁴ Any ETC that receives support from the State Universal Service Fund will utilize that support for the provision, maintenance, and upgrading of facilities and services for which the support is intended -- universal service offered at reasonable and comparable rates.

C. The Proposed Rate Design Structure Establishes a Rational Framework to Accommodate Industry Change That Is Consistent With The Public Interest and the Policy Established by both the Tennessee Act and the Telecommunications Act of 1996.

In order to achieve the objective of providing a flexible regulatory structure responsive to the varying needs and characteristics of the Tennessee rural Independents and their customers, the Tennessee Universal Service Rate Redesign Plan provides for the implementation of rational and administratively efficient rate structures together with associated tariffs.

The Tennessee Universal Service Rate Redesign proposal provides for the transition of each rural company's intrastate access charges to parity with its interstate access rates. When this proposal is approved by the Authority, each rural Independent would reduce its intrastate switched access charges to parity with its interstate access rates concurrent with the implementation of the resulting required funding from the State USF. In addition and to the extent that additional adjustments in a rural ETC's interstate access charges are subsequently implemented, such adjustments will be applied to the rural Independent's intrastate access charges on January 1 of the following calendar year. The additional differential between a company's base year intrastate revenues and the level of revenues generated by the application of the adjusted access rates will be recovered through funding from the State USF. By making these intrastate access rate adjustments, each rural ETC's intrastate access charges will be maintained at parity with their interstate access

²⁴ While the Coalition anticipates that most telecommunications carriers would base the recovery of this State USF funding obligation on a percentage applied to intrastate service retail charges (i.e., a surcharge), the Coalition would not object if the Commission were to require all local exchange carriers, including local competitive service providers, to meet their respective funding requirement by assessing a flat monthly State USF Charge to all end users.

charges. In all other respects, the rural ETCs will concur in the terms and conditions of their interstate access tariffs.

D. Conclusion

There are two significant objectives to the Tennessee Universal Service Rate Design Restructuring Plan proposed by the Tennessee rural Independents. The first objective is to ensure that all companies have the opportunity to implement rate designs that are reasonably comparable to rates charged for similar services in urban areas -- this applies to both customer service rates and access rates.

The second objective of the plan is to provide for the implementation of a State USF which is an essential element in ensuring the availability of cost recovery under the proposed rate design that results in a reduction in access charges and the maintenance of basic universal service dialtone service rates at levels that are reasonable and comparable to those charged by non-rural LECs.

Accordingly, the Tennessee rural ETCs respectfully submit that the Tennessee Universal Service Rate Redesign proposal will serve the public interest, and respectfully requests that the Authority adopt the proposal described herein.

IV. The Impact of BellSouth's Unilateral Cancellation of IntraLATA Settlement Contracts With the Independents on Universal Service and Request For Intervention by the Authority.

In its "*Order Opening Docket For Purpose of Addressing Rural Universal Service and Appointing Hearing Officer*" (hereafter, "*Order Opening Docket*") issued on July 14, 2000, in this proceeding, the Authority demonstrated its awareness of the universal service concerns that arise as a result of proposed, potentially arbitrary changes in the treatment of intraLATA toll service between the Independents and BellSouth. Specifically, BellSouth has notified each Independent of its intent to terminate the existing arrangements as of January 1, 2001. The Authority has noted:

While retail intraLATA toll rates have declined since the divestiture of AT&T, these settlements have maintained the stability of Independent ILECs during such decline. If

BellSouth does withdraw the current settlement agreements, the Independent ILECs' earnings may decrease resulting in pressure on local rates.²⁵

The Authority's observation is correct; rural Independent telephone companies have relied upon the existing contract arrangements and the resulting, relatively more significant levels of cost recovery provided by access charge payments. BellSouth has established statewide average intraLATA toll rates in compliance with its lawful obligations. Each Independent has provided originating and terminating access service with respect to the intraLATA toll service offered pursuant to the established BellSouth tariffs. In return, the Independents have been compensated for their origination and termination of this toll calling in accordance with the established contractual arrangement with BellSouth.

Prior to transmitting notification of its intent to cancel the existing contractual arrangements, BellSouth representatives and representatives of the members of the Coalition met to discuss the concerns of BellSouth that have lead to its decision to terminate the agreements. Consistent with the facts noted by the Authority in the *Order Opening Docket*, the Independents informed BellSouth that they could not join BellSouth in bilaterally altering the existing arrangements in the absence of TRA participation. As understood by the Authority, the existing arrangements have been relied upon by the Independents as part of an overall rate design and universal service cost recovery plan in Tennessee. Arbitrary or precipitous change in one aspect of these mechanisms cannot be achieved in a vacuum.

The Independents have estimated the impact of the proposed termination of the existing intraLATA toll arrangements with BellSouth. In the aggregate, implementation of the BellSouth proposal equates to a revenue loss of \$15.4 million.²⁶ In the absence of the State USF mechanism

²⁵ *Order Opening Docket*, p. 3.

²⁶ This loss of revenues would result in an equivalent expense savings for BellSouth.

proposed by the Coalition, this revenue dislocation translates to \$4.10 per access line per month, on average for the 20 Coalition members.²⁷ The median impact for the 20 Coalition members is approximately \$4.74 per month per access line.

BellSouth's potential arbitrary termination of existing arrangements and the resulting financial impact together demonstrate the need for the implementation of the Coalition proposal for a State USF and the related rate redesign. Until now, cost recovery for universal service in the rural company areas has been significantly dependent on the existing contract arrangements and the resulting access related revenue. In the absence of these arrangements, each company's costs would have to be recovered from an alternative source or the rural company could not sustain its existing level of universal service investment and operations. The only alternative cost recovery source currently available would be increases in basic service rates. The quantitative analysis undertaken by the Independents, however, demonstrates that the resulting rural customer rates would not be comparable to the established level of rates in Tennessee for an equivalent level and scope of service.

The Independents have suggested to BellSouth that the public interest demands that potential changes in existing intraLATA arrangements should be made only in the context of this proceeding. As set forth in Section III above, the Coalition's universal service and rate redesign proposal recognizes that, in the long term, movement from existing settlement levels to access charges at parity with interstate access charges will serve the public interest if the change is made as part of an overall comprehensive plan addressing universal service requirements. Arbitrarily reducing each Independent's intraLATA toll revenue source for cost recovery may serve BellSouth's interest, but it most clearly will not serve the public interest, in general, or the universal service needs of rural

²⁷ The effect of potential reductions in interLATA access rates would raise this impact to \$5.47, on average.

Tennessee subscribers.

BellSouth established its existing intraLATA toll tariffs with full knowledge of the cost of the existing settlements arrangements. BellSouth pursued alternative price regulation with the TRA with the existing arrangements in place. The Independents have submitted to BellSouth, and now respectfully submit to the TRA, that there is no basis, need, or lawful requirement to alter the existing arrangements arbitrarily or precipitously prior to the TRA's consideration of this proceeding and the establishment of a replacement plan. In fact, the Coalition's Universal Service and Rate Redesign Proposal offers a rational basis for all parties to proceed in a manner that both addresses BellSouth's individual company concerns while fully addressing the universal service concerns of all Tennessee rural ratepayers.

The BellSouth January 1, 2001 termination date will fast approach. If BellSouth proceeds to terminate the existing arrangements arbitrarily and to withhold settlements from the Independents, many of the rural companies will quickly find their existing operations unsustainable as a result of reduced cash flow. Accordingly, the Independents respectfully request TRA intervention in this matter and ask that the Authority direct BellSouth to maintain the existing division of intraLATA toll revenues, in accordance with the currently effective contractual arrangements, pending the outcome of this proceeding. Because of the severe ramifications of the termination of these arrangements that BellSouth wants to effectuate on January 1, 2001, the Independents further respectfully request expedited consideration of this emergency request.

V. Conclusion

The Coalition welcomes and appreciates the Authority's consideration of the establishment of a rural State Universal Service Fund mechanism consistent with the policies and requirements of both the Tennessee Act and the Federal Act. The Authority, like the FCC, has appropriately recognized that consideration of universal service in rural company service areas warrants distinct

treatment from non-rural companies. Unlike larger companies with diverse service areas, the rural companies serve areas with higher cost to serve and low density characteristics that are not subject to similar market forces. Cost models do not predict the individual real life investment and operational requirements of these service areas.

In order to maintain affordable basic rates in the rural company service areas, cost recovery has traditionally relied on toll service as a revenue source, including both traditional toll settlements and access charges. The resulting rate design not only reflected nationwide universal service considerations, but it also reflected an implicit regulatory decision with respect to how the costs of the rural network would be recovered. The decision to weight cost recovery towards toll services reflected an understanding of the value of the rural network -- the value was reflected not only in the benefits to rural subscriber, but also in the benefits to all other subscribers who could place and receive calls from users in rural area.

The pressure for change in this traditional rate design and cost recovery methodology is a natural byproduct of both technological and regulatory changes. Long distance carriers, required to provide geographically average toll rates, seek to reduce their access expenses by lowering rural company access charges. The BellSouth unilateral intent to terminate existing intraLATA toll arrangements is a vivid demonstration of this pressure and the ramification on the provision of universal service. Concurrently, the rural companies face the challenge of meeting increasing investment requirements to provide advanced services (*e.g.*, broadband) and maintain compliance with regulatory requirements (*e.g.* CALEA).

In the presence of each of these individual changes and pressures, the rural companies, federal regulators, and state regulators must continue to meet both federal and State universal service mandates. The achievement of these objectives requires refocused attention on the fundamental policy basis for the prior existing rate design and cost recovery mechanisms: The rural service area

network is valuable to both the subscribers that reside in the rural area and the subscribers that are on the other end of the communications. It is this value -- the value of the network to all subscribers -- that provides a sound policy basis to the universal service fund mechanisms that are addressed by both the Federal Act and the Tennessee Act.

On the basis of this foundation, the rural Independent Companies respectfully offer their proposal for a Tennessee Universal Service and Rate Redesign Plan. The implementation of this proposal will foster the provision of universal service at reasonable, affordable, and comparable rates to subscribers in rural Tennessee and the continued availability of advanced and advancing services to all users. At the same time, the plan will provide for the establishment of access charges at a rational level that will encourage the provision of competitive toll services throughout the State. The universal service fund established by this plan will ensure the ability of rural companies to recover the costs of providing universal service while maintaining the reasonable and comparable levels of rates for basic service and access. All Tennessee telecommunications service providers and their end user customers will contribute on a competitively neutral basis to the state USF, reflecting the value to all ratepayers of universal service connectivity to the rural service areas of the State.

Accordingly, and the Coalition respectfully requests that the Authority adopt and implement the proposed rural Universal Service and Rate Redesign Plan. In addition, the Coalition respectfully requests that the TRA direct BellSouth to maintain the existing arrangements between BellSouth and

the Independents with respect to intraLATA toll until the matters before the Authority in this proceeding are resolved.

Respectfully submitted,

**The Tennessee Rural Independent
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CERTIFICATE OF SERVICE

I hereby certify that on September 5, 2000, a copy of the foregoing document was served on the parties of record, via the method indicated:

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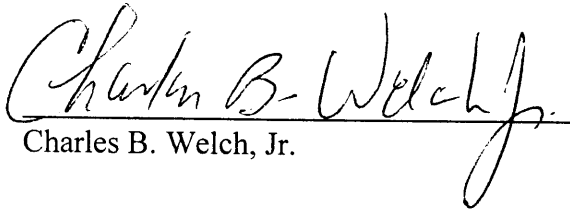
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